

May 30, 1997

Mr. Carl Masaki
Forestry Program Manager
Division of Forestry and Wildlife
Dept. of Land & Natural Resources
1151 Punchbowl Street, Room 375
Honolulu, Hawaii 96813

Dear Mr. Masaki:

Use of Foreign-Trade Zone procedures are potentially beneficial to an integrated wood processing industry in Hawaii. The staff at Hawaii Foreign-Trade Zone No. 9 actively pursues expansion of this economic development program and is readily available to discuss its benefits with all interested parties.

Traditional milling operations have changed in recent years to allow products such as fiberboard and pressed woods to be produced. These new milling operations make use of duty-bearing inputs such as adhesives to produce high-value products. Related to this is a trend in the wood industry to integrate harvesting, milling, and distribution activities on an international level.

The future of Hawaii's forestry industry includes the location of processing facilities on the Hamakua coast on the island of Hawaii. The Hawaii Foreign-Trade Zone program can allow international companies to better integrate a processing facility in Hawaii with other operations. A preliminary analysis indicates that many types of wood manufacturing operations do have a foreign-trade zone benefit.

A summary of potential foreign-trade zone benefits include:

Duty Savings. The 4%-6.8% duty on virtually all common wood adhesives would be avoided on all exports from the Hawaii facility. Depending upon the manufacturing approval granted by the Foreign-Trade Zones Board, this savings could be extended to merchandise entering domestic commerce as well. For domestic entries, at the very least, duty would be postponed until the final goods left the manufacturing plant for the retail market.

Differences in duty rates between inputs in the manufacturing process and the final goods translate into savings for a wood manufacturer. For example, a typical plant making medium-density fiberboard (duty rate of 1.2% to 1.6%) may use wood chips from Hawaii (free) and domestic and foreign wood adhesives (4% - 6.8%). Because a foreign-trade zone is considered outside of the United States, formal Customs entry is postponed until the end of the manufacturing process. At this time duty is assessed at 1.2% for amount of wood adhesive (and any other duty-bearing item) used in the manufacturing process. In this example the wood manufacturer is able to reduce input cost by up to 5.2%.

Integration. The special status of foreign-trade zones allows seamless integration between international wood harvesting, processing, and distribution schemes. By being part of a foreign-trade zone, a company is protected against impediments like quotas and other trade restrictions. For example, to cover gaps in the local supply of logs, wood material can be imported or brought in from the mainland. Investors can have the assurance that logs and other inputs can flow through Hawaii without meeting any costly interruptions. The bottom line: foreign-trade zone status will insure that a company will be able to use any mix of domestic and foreign woods, adhesives, and other inputs in a processing facility in Hawaii.

Cost environment. The Foreign-Trade Zone program alone can have a dramatic effect on a company's cost environment by allowing the simultaneous use of domestic and foreign inputs and reducing Customs-related transaction costs. As part of the state Department of Business, Economic Development & Tourism, Foreign-Trade Zone No. 9 works to ensure that manufacturing operations receive all available federal, state, and local incentives when they establish operations in Hawaii.

The United States produces many of these adhesives discussed above, and, in many cases, could be the low-cost provider. Japan, Taiwan, Canada, Mexico, and China are also low-cost providers of adhesives. What foreign-trade zone procedures can support is an international sourcing approach that provides flexibility and price

stability. Often, foreign companies have agreements with subsidiaries and suppliers that foreign-trade zone procedures can accommodate.

Mr. Carl Masaki

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I would like to personally invite any company considering setting up a wood manufacturing operation in Hamakua on the Big Island of Hawaii to contact us for a clear discussion on how the foreign-trade zone program may apply to their company.

Sincerely,

Gordon M. Trimble
FTZ Administrator

The Foreign-Trade Zone Program and Wood Manufacturing in Hawaii

State of Hawaii
Department of Business, Economic Development & Tourism
Foreign-Trade Zone Division

Executive Summary

- | Why use a foreign-trade zone?
- | Types of processing activity
- | Calculating the basic savings
- | Duty rates for common wood adhesives
- | A schematic overview of an FTZ wood manufacturing operation
- | Experience: current activity
- | Conclusion

Why Use a Foreign-Trade Zone?

- | **The FTZ program reduces the cost of production by allowing the use of foreign inputs in a “duty-free” environment**
- | **Insures a seamless fit for a Hawaii facility into a larger wood supply and processing scheme**
- | **Flexibility, security, exemption from some local taxes--the best possible production environment**
- | **Ability to use both domestic and foreign sources of materials simultaneously**

Types of FTZ Activity

- | Autos
- | Oil refineries
- | Pharmaceutical
- | Office equipment
- | Computers/
Telecommunications
- | Shipyards

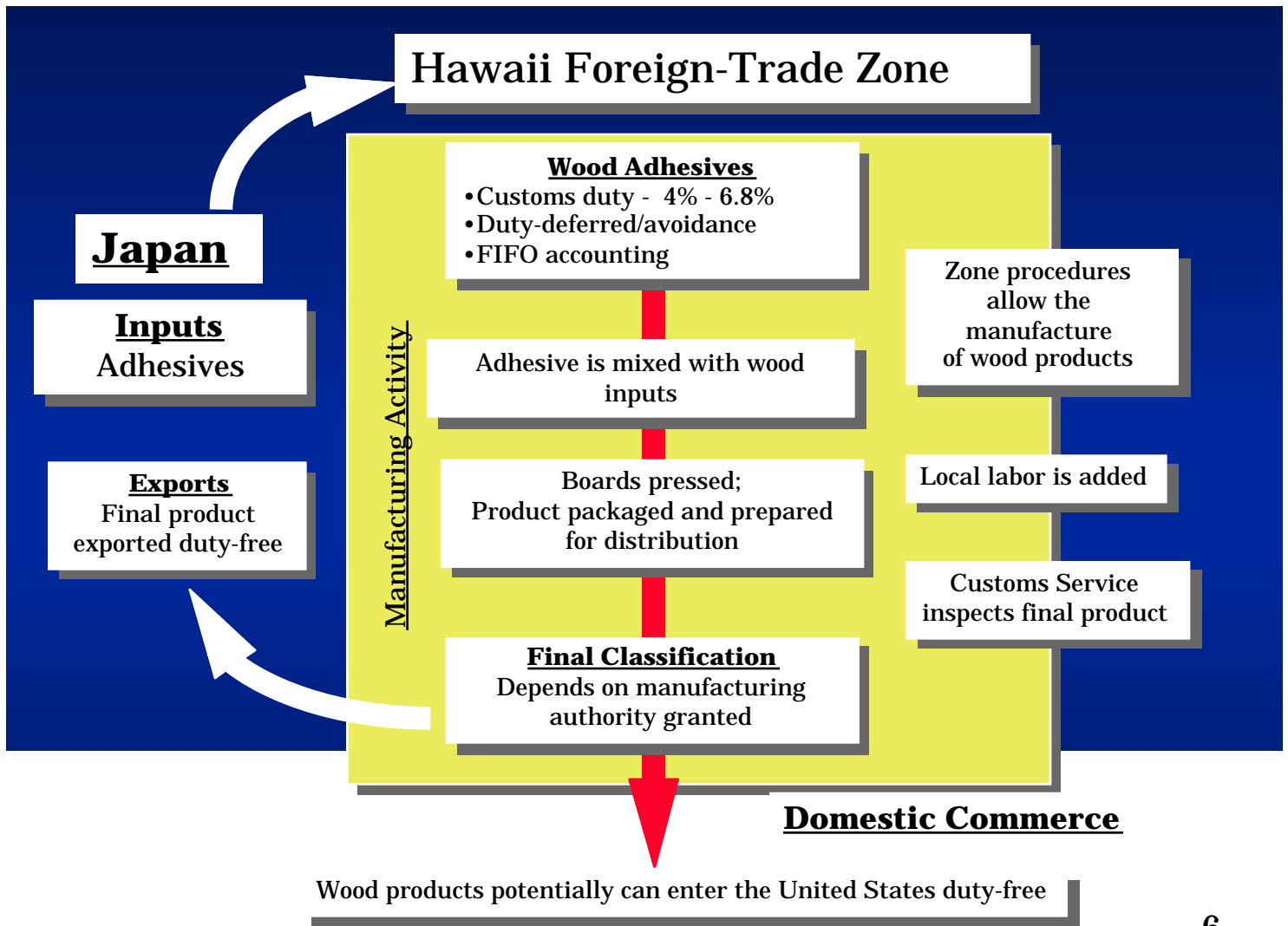
- | Food processing
- | Appliances
- | Chemical
production
- | Apparel/Footwear
- | Power/Hand tools
- | Marine systems

Calculating the Basic Savings

Does a foreign-trade zone benefit exist for a wood manufacturing operation?

- 4 Is a portion of the company's sales exports?
- 4 Does the operation integrate internationally?
- 4 Will foreign-sourced logs be used periodically?
- 4 Are foreign inputs (adhesives) less expensive than domestic inputs?
- 4 Are foreign inputs being purchased through a domestic vendor?
- 4 Is there a difference in tariff rates between the inputs and the final product?
- 4 Are any of the ingredients used in the manufacturing process subject to a quota?

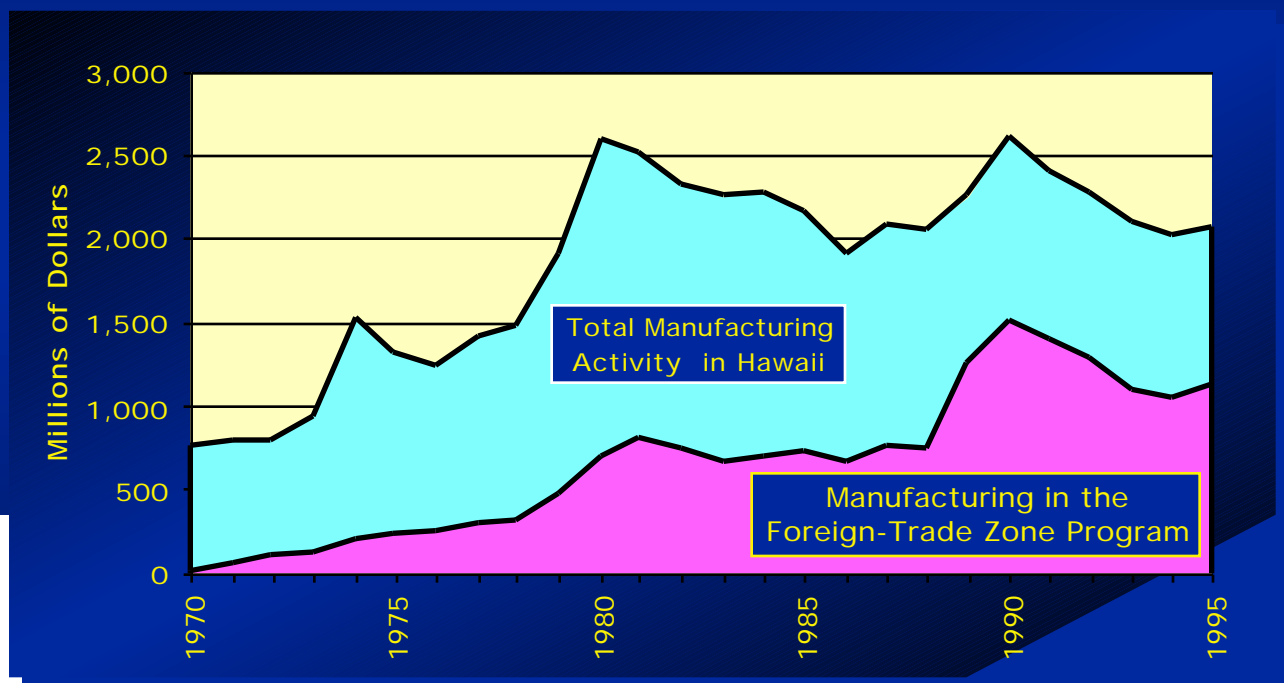
A "yes" answer to any of these questions means an FTZ benefit could exist.



Experience: Processing Activity for 1996

- | \$2.13 billion in merchandise handled
- | Exports of \$339.9 million
- | \$144 million of value-added activity
- | Employment of 1,573 workers

Experience: Manufacturing in Hawaii Under Zone Procedures



Conclusion

- | **The Hawaii Foreign-Trade Zone will work with individual companies to determine if a foreign-trade zone benefit exists**
- | **If a benefit does exist, we will commit to undertaking the cost of the application process**
- | **As a state development program our primary goal is to increase the amount of value-added activities in Hawaii**